No. 83-211

IN THE

Supreme Court of the United States

October Term, 1983

LUCILE LOWRY and LOWRY-ZWEIG CORP.,

Petitioners,

vs.

THE BALTIMORE & OHIO RAILROAD COMPANY,
THE CHESAPEAKE & OHIO RAILROAD COMPANY,
and CHESSIE SYSTEM, INC.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

PETITIONERS' REPLY BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

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Petitioners submit this Reply Brief in response to issues raised in respondents' Response to Petition.

I. RESPONDENTS' CHALLENGE TO THE THIRD CIRCUIT'S HOLDING ON § 10(b) LIABILITY IS NOT PROPERLY BEFORE THIS COURT IN THE ABSENCE OF A CROSS-PETITION

Respondents invite this Court to deny certiorari with respect to the questions presented in the Petition, yet "grant review of this matter to affirm that there has been no violation of the

securities laws by the [respondents]." Resp. Br. p. 8. They have failed, however, to file a cross-petition which seeks this relief.

It has been consistently held that issues not raised in a petition or cross-petition for certiorari are not properly before the Court. *Lake Country Estates v. Tahoe Planning Agency*, 440 U.S. 391, 398 (1979). This doctrine is exemplified by *Federal Energy Administration v. Algonquin SNG, Inc.*, 426 U.S. 548, 560 n.11 (1976), where the respondents sought modification of the judgments below without cross-filing for certiorari. The Court held that because of such failure to cross-petition, respondents were "at this point precluded from seeking such modification." 426 U.S. at 560 n.11. Similarly, in *United States v. O'Brien*, 391 U.S. 367 (1968), the Government petitioned for certiorari and the defendant cross-petitioned but also briefed issues raised in neither the petition nor the cross-petition. This Court stated flatly, "[T]hose issues are not before the Court." 391 U.S. at 386 n.31.

Respondents here seek wholesale reversal of the Circuit Court's liability ruling. Such an objective may only be accomplished through the certiorari process. The attempt to circumvent that process should be rejected.

II. RESPONDENTS ARE COLLATERALLY ESTOPPED FROM RELITIGATING THE ISSUE OF § 10(b) LIABILITY

As detailed more fully in the Petition, whether petitioners have a federal claim turns on two discrete questions: (1) Did respondents violate § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b)? (2) If so, was a claim based on that violation assigned to petitioners by operation of law?

The first of these questions was put to rest by the decision in *Pittsburgh Terminal Corp. v. The Baltimore & Ohio R.R. Co.*, 680 F.2d 933 (3d Cir. 1982), an action which challenged precisely the same transaction as the case at bar and which was consolidated with this case on appeal. In *Pittsburgh Terminal*, the Third Circuit held that respondents' concealed dividend did violate § 10(b). Respondents sought *in banc* review, which was denied, and then petitioned this Court for a writ of certiorari,

which was also denied. *See* Supreme Court Docket Nos. 82-620; 82-622; 103 S.Ct. 476 (1982). Accordingly, assignment, *vel non*, is the only issue properly presented to this Court—primarily whether the court below was empowered to dismiss the § 10(b) claim in spite of the even division among the judges on the question of assignment and the District Court's refusal to dismiss for lack of an express assignment. *See* Pet. at pp. 7-12.

Notwithstanding the finality of the ruling on § 10(b) liability, respondents seize upon the Petition as an invitation to resurrect that foreclosed issue. The doctrine of collateral estoppel precludes wasteful relitigation of decided issues. In *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 326 (1979), the Court observed that collateral estoppel "has the dual purpose of protecting litigants from the burden of relitigating an identical issue with the same party or his privy and of promoting judicial economy by preventing needless litigation." *Accord, Blonder-Tongue Laboratories, Inc. v. University of Illinois Foundation*, 402 U.S. 313, 328-29 (1971).

It is plain that all the requisites for application of collateral estoppel laid down by this Court in *Parklane Hosiery, supra*, 439 U.S. at 329-31, are satisfied here. First, petitioners did not seek to avoid being bound by a possible adverse judgment in *Pittsburgh Terminal* while retaining the right to exploit a favorable one. Consolidation at the District Court level was attempted but denied because *Pittsburgh Terminal*, which had been filed before *Lowry*, was ready for trial whereas *Lowry* was not. Later, at petitioners' instance, the cases were consolidated on appeal. Second, respondents were not required to litigate *Pittsburgh Terminal* in a forum where their rights to discovery, to call witnesses or to otherwise fully present their case were limited in any way. Third, respondents had sufficient financial stake in the *Pittsburgh Terminal* action (plus knowledge of the *Lowry* claims) to vigorously defend the action—as indeed they have. Finally, there are no prior judgments inconsistent with *Pittsburgh Terminal*.[1]

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[1] The Court of Appeals remanded *Pittsburgh Terminal* to the District Court for a determination of "appropriate relief." 680 F.2d at 943. This remand for a (footnote continued)

Under these circumstances, there can be no doubt that collateral estoppel foreclosed respondents from relitigating their § 10(b) liability in the court below. Four of the six judges below who held for § 10(b) liability[2] regarded the panel's *Pittsburgh Terminal* liability ruling as controlling this case.[3]

Respondents have had their day, indeed many days, in court on the liability issue. True, as decided in *Pittsburgh Terminal*, liability might conceivably be reviewed by this Court at some later stage *of that action*, as suggested by cases cited at p. 4 n.2 of the Response. It in no way follows, however, that this Court should be called upon, *in this case*, to reverse a fully litigated determination in the earlier lawsuit. Such an undertaking could not co-exist with the collateral estoppel principle and policy fashioned by this Court and quite consistently understood and applied by courts below.

III. RESPONDENTS' "ADVICE OF COUNSEL" DEFENSE IS MERITLESS

We here address respondents' primary defense against § 10(b) liability, assuming, without in any way conceding, that that issue is properly presented in the absence of a cross-petition for certiorari and in light of the final liability determination in *Pittsburgh Terminal*, a discussed under Points I and II above.

Respondents contend that their "good faith reliance on the advice of counsel" precludes a finding of scienter, and hence liability under § 10(b). While reliance upon the advice of counsel might constitute a valid defense in some circumstances, to

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limited purpose does not, of course, affect the finality of the holding on § 10(b) liability. *Lummus Co. v. Commonwealth Oil Refining Co.*, 297 F.2d 80, 89 (2d Cir. 1961), *cert. denied*, 368 U.S. 986 (1962); Restatement, Judgments (2d) (1982) § 13, Comment g (and Reporter's Note thereto, p. 141, citing cases from other Circuits which have adopted the *Lummus* rule).

[2] Gibbons, Garth, Sloviter, Adams, C.J.J.

[3] Chief Judge Seitz and Judge Becker, who also held for § 10(b) liability, expressed concurrence in the substance of *Pittsburgh Terminal's* liability ruling and found it unnecessary to decide whether it bound the court sitting *in banc*.

so hold on the facts of this case would mark the effective repeal of § 10(b).

It is undisputed that advance notice of the MAC dividend was intentionally withheld by respondents so that their public debenture-holders would have no chance to convert and thus share in that dividend. The injury to debenture-holders—loss of the opportunity to convert into B&O stock which included the valuable non-rail assets; *see* Pet. at 4—was both substantial and plainly forseeable.

Prior to effecting this scheme, respondents sought the advice of Robert F. Hochwarth, an attorney-employee of B&O. Another B&O employee, Roland Donnem, was also consulted. *See* Resp. Br. at 5-6. Both approved the transaction. Respondents concede, however, that "neither Hochwarth nor Donnem specifically considered whether notice had to be given pursuant to Rule 10b-17 [17 C.F.R. § 240.10b-17], the Third Circuit's predicate for liability in the *Pittsburgh Terminal* case. . . ." Resp. Br. at 7. Furthermore, at no time was independent outside counsel asked for an opinion on the legality of the transaction.[4]

In *Fogel v. Chestnutt*, 533 F.2d 731, 749 (2d Cir. 1975), *cert. denied*, 429 U.S. 824 (1976), Judge Friendly was confronted with an analogous defense based upon reliance on the informal advice of inside counsel. He held:

> Reliance on such obviously casual advice from a lawyer having a personal stake adverse to the shareholders affords no protection unless it is right—in which event it is unnecessary to assert the defense of reliance.

Here, respondents seek § 10(b) immunity based on the advice of their own employees which was concededly rendered without

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[4] Hochwarth did ask a "senior partner" of Hunton & Williams to "let me know if you see any problems with this procedure," and no objection was forthcoming. Resp. Br. at 6. But there is no evidence that aside from this casual request and subsequent silence, Hunton & Williams was ever requested to, or did, research the law. Certainly, no written (or even verbal) opinion was rendered. To call such silence the "advice of counsel" and then raise it as a shield against § 10(b) liability is patently untenable.

consulting the relevant law. If such casual advice from affiliated attorneys were enough to protect one from § 10(b) liability, it would be hard to imagine an instance where a corporation could not grant itself immunity from prosecution by the simple expedient of having one of its own employees render a suitable opinion without even researching the law. Obviously, Congress could not have intended that § 10(b) be so easily avoided.[5]

IV. THE CIRCUIT WAS EQUALLY DIVIDED ON THE PIVOTAL ASSIGNMENT ISSUE, FOR WHICH REASON THE DISMISSAL OF FEDERAL CLAIMS SHOULD NOT STAND

Judge Gibbons, in his able and caustic dissent from the "Per Curiam Opinion of the Court" in this case, had this to say, among other things, concerning the integrity of that result:

> [T]he method by which the court arrived at a judgment is fundamentally inconsistent with sound appellate practice in the courts of appeals and will bring this court into disrepute.
>
> * * *
>
> I would regard any effort to apply res judicata effect to a class action judgment predicated upon the concurrence of two legal propositions, neither of which commands a majority in the court which announced the judgment, to be a violation of due process of law.
>
> * * *
>
> Thus, this court's willingness to enter a judgment based on two propositions neither of which commands

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[5] Indeed, if respondents are correct, then in-house counsel, not the courts, will become the final arbiters of what actions constitute a violation of the securities laws.

Respondents' related argument, Br. at 12, that Rule 10b-17 contravenes the *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976), requirement of scienter, overlooks that the *Pittsburgh Terminal* panel, 680 F.2d at 942, under the heading "*Scienter*", explicitly addressed that issue and found that respondents' conduct amply fulfilled the *Hochfelder* requirement.

> a majority has accomplished nothing except to bring its appellate process into disrepute.
>
> * * *
>
> The entry of a judgment based on two legal propositions, neither of which commands a majority, is a disgrace to the judicial process.

(30a, 40a, 50a).

And further, in his "Statement re Denial of Petition for Modification of Judgment":

> [I]f the Supreme Court is concerned about public perceptions as to the integrity of the federal appellate process, it should grant certiorari in this case and formally vacate the unsupportable judgment of this court.

(70a-70.1a).

Respondents' attempt to justify the Per Curiam Opinion boils down to these unfounded assertions:

A. The assignment issue (according to Respondents, Br. at 13, 14-15) was not properly before the Circuit since no party appealed the District Court's order denying defendants' first summary judgment motion (which explicitly challenged plaintiffs as late purchasers of the debentures (66a)). In actuality, the assignment question was fully briefed for the Circuit by both sides with no suggestion by respondents that the issue was not properly before the court; and the assignment question was virtually the court's sole preoccupation at the *in banc* rehearing where supplemental briefs were requested and filed on six issues relating solely to assignment (6a-7a).

B. The Per Curiam Opinion and Judgment should stand because (according to Respondents, Br. at 13-14, 16) appeals are taken from judgments, not from their reasoning; and, out of the eight sitting judges, two voted against liability and three voted against automatic assignment, making "a majority" of five for dismissal and affirmance. This of course overlooks, as stressed

by dissenting Judge Gibbons, that the purported majority consists of a minority on the liability question and half of the deadlocked six who addressed the assignment question, so that the result is utterly meaningless in terms of a meeting of a majority of judicial minds on any relevant issue or proposition.

Respondents, Br. at 16 n.10, cite four cases supposedly supportive of "the weird judgment in this case" (49a). None of those citations is remotely in point because none of them attained "a majority" by pooling minority votes on discrete, entirely unrelated issues, as in this case.

Thus, *Furman v. Georgia*, 408 U.S. 238 (1972), reversed the death sentences of three convicts, on the separate opinions of five Justices who concurred that the sentences were unconstitutional, although for differing reasons. In the infamous *Dred Scott v. Sandford*, 19 How. (60 U.S.) 393, 15 L.Ed. 691 (1856), seven Justices agreed that Scott was still a slave, the division within the majority was solely on whether the decision below, against Scott, should be affirmed on the merits or whether his complaint should be dismissed because he was not "a citizen" constitutionally entitled to sue in a court of the United States. In *Smith v. U.S.*, 5 Pet. (30 U.S.) 292, 8 L.Ed. 130 (1831), judgment was reversed on the strength of a plurality of minority opinions on the inauthenticity of the critical documentary evidence—again a single issue. *Marks v. U.S.*, 430 U.S. 188 (1977), respondents' fourth and last case, presumably is cited for a quoted dictum with no discernible application to the present Petition.

V. THE § 10(b) CLAIMS WERE ASSIGNED TO PETITIONERS BY OPERATION OF LAW

Respondents rely heavily on one District Court case, *Independent Investment Protective League v. Saunders*, 64 F.R.D. 564 (E.D. Pa. 1974), where, as noted in the Petition, p. 18 n.16, the assignment issue was inadequately presented to the court. Left unexplained by respondents is why federal receivership claims should travel with the bonds (as *Phelan v. Middle States*

Oil Co., 154 F.2d 978 (2d Cir. 1946) held) while federal securities law claims should not (as respondents would have it).

Respondents contend that automatic assignment would violate the "in connection with" requirement of § 10(b) discussed in *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975). This argument proves too much; it would impugn *express* assignments as well (which even respondents concede are appropriate under § 10(b); *see* Resp. Br., pp. 17, 18 n.12). The related argument—that one could never know whether a prior holder had been fraudulently induced to purchase or sell his security; Resp. Br., p. 18—is inapposite in this case. Every B&O debenture-holder on December 13, 1977, the date of respondent's violation, was thereby defrauded. Automatic assignment avoids not only the formidable problems associated with tracing bearer securities (Pet., pp. 15-16), but also eliminates any possibility of double liability (*i.e.*, under state law to transferees and under respondents' view of federal law, to the original holders; Pet. 9, text and n.11)—two points which respondents do not address.

Respondents find it "curious" that the Petition makes no mention of N.Y. Jud. L. § 489 (McKinneys 1968) ("Purchase of claims by corporations and collection agencies"). No mention was made of this penal statute because it has no application to this case or the questions presented for review. Petitioner, Lucile Lowry, is neither a corporation nor a person engaged in the "business of collection and adjustment of claims." Accordingly, the statute has no effect whatsoever upon her claims, Petitioner, Lowry-Zweig Corp., though a corporation, is not in the collection business and did not purchase the B&O debentures for the sole purpose of bringing suit thereon, as New York law would require before § 489 becomes operative. *Sprung v. Jaffe*, 3 N.Y.2d 539, 544 (1957). In any event, whether § 489 comes into play here is a factual issue (*Fairchild Hiller Corp. v. McDonnell Douglas Corp.*, 28 N.Y.2d 325, 330 (1971)), never reached below and not before this Court now.

CONCLUSION

For the reasons stated above, and in the Petition, this Court should grant certiorari and reinstate petitioners' § 10(b) claim. Alternatively this Court should grant certiorari and rule upon the assignment issue.

Dated: New York, New York
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Respectfully submitted,

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